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IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

1616 REMINC LIMITED PARTNERSHIP,
Petitioner,

v.

UNITED STATES ELEVATOR CORPORATION,
Respondent.

Petition for a Writ of Certiorari to the United States Court of Appeals for the Fourth Circuit

BRIEF AND APPENDIX FOR PETITIONER

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QUESTIONS PRESENTED

1. In a proceeding under the Bankruptcy Act of 1898, is United States Bankruptcy Rule 810 unconstitutional to the extent that it precludes de novo review by an Article III judge of a common law contract claim against the debtor?

2. Can oral testimony concerning a damaging admission render harmless the bankruptcy referee's improper exclusion from evidence of the document in which the admission originally appeared?

3. Is the assignee of a right of recovery against a contracting party affirmatively liable to that party for an obligation of the assignor where the assignment expressly did not include any of the assignor's obligations?

4. May a party recover a general unsecured claim against a bankruptcy debtor where the claim against the debtor did not arise until after the debtor filed a petition in the United States Bankruptcy Court and where the claim does not relate to a post-bankruptcy extension of credit?

PARTIES

Petitioner 1616 Reminc Limited Partnership is a limited partnership organized under the laws of Virginia. The general partners are Theodore B. Gould, an individual and Washington Properties, Inc., a Michigan Corporation. Respondent is United States Elevator Corporation.

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BRIEF AND APPENDIX FOR PETITIONER

OPINIONS BELOW

None of the opinions below has been reported. The memorandum opinion of the United States Bankruptcy Court appears in the Appendix at pages 7a-38a. The oral opinion of the United States District Court appears in the Appendix at pages 4a-5a. The unpublished opinion of the United States Court of Appeals appears in the Appendix at pages 1a-3a.

JURISDICTION

The judgment sought to be reviewed was entered by the United States Court of Appeals for the Fourth Circuit on June 10, 1982. Jurisdiction of this Court is invoked under section 1254(1) of Title 28, United States Code.

CONSTITUTIONAL PROVISION AND RULE INVOLVED

United States Constitution, Article III, Section 1:

> The judicial Power of the United States, shall be vested in one supreme Court, and in such inferior Courts as the Congress may from time to time ordain and establish. The Judges, both of the supreme and inferior Courts, shall hold their Offices during good Behaviour, and shall, at stated Times, receive for their Services, a Compensation, which shall not be diminished during their Continuance in Office.

United States Bankruptcy Rule 810:

> Upon an appeal the district court may affirm, modify, or reverse a referee's judgment or order, or remand with instructions for further proceedings. The court shall accept the referee's findings of fact unless they are clearly erroneous, and shall give due regard to the opportunity of the referee to judge of the credibility of the witnesses.

STATEMENT OF THE CASE

This is a proceeding under the Bankruptcy Act of 1898 in which respondent United States Elevator Corporation ("USE") asserted a claim against the debtor, petitioner 1616 Reminc Limited Partnership ("Reminc"), for the balance due on a construction contract. Reminc, in turn, asserted a breach of contract counterclaim against USE.

USE had, on March 16, 1973, contracted with Citcon Corp. ("Citcon") to design, construct, and install an elevator system in the Xerox Building, located at 1616 North Fort Meyer Drive in Rosslyn, Virginia. Citcon was, at that time, the general contractor responsible for Xerox Building construction. The building owner was Reminc, a limited partnership. Memorandum Opinion, 1-2 (App. 8a).

On August 15, 1975, Reminc filed a petition initiating proceedings before the United States Bankruptcy Court. On May 19, 1976, the Bankruptcy Court approved pursuant to Chapter XII of the Bankruptcy Act a plan of arrangement. Under the plan, Reminc was to remain a debtor-in-possession and attempt to operate the Xerox Building as a profitable commercial venture. *Id.* (App. 7a-8a).

In accordance with the plan of arrangement, Reminc wound up its contractual relationship with Citcon. Reminc then had Citcon assign to it such rights of action for latent construction defects as Citcon may have had against its subcontractors. A single writing assigning to Reminc Citcon's rights of action against all Xerox Building subcontractors was executed on August 6, 1976. PX 10 (App. 55a).

The proceeding now before the Court began when USE filed an Amended Complaint asserting a claim against Reminc for the balance of payments due to USE under its subcontract with Citcon (App. 41a). The sole basis for liability alleged in the Amended Complaint was a mechanic's lien filed by USE against the Xerox Building. Reminc, alleging that USE did not perform its obligations under the subcontract, and that the elevator system required substantial remedial construction, counterclaimed for $1.500,000. (App. 45a).

The Bankruptcy Court ruled, on January 15, 1977, that a waiver of the mechnic's lien executed by USE was valid and binding. *See* Memorandum Opinion, 2 (App. 8a). This ruling was affirmed by the District Court. Rather than appeal the ruling further, USE abandoned the mechanic's lien and moved the Bankruptcy Court to recognize an unsecured claim against the debtor based exclusively on the assignment from Citcon to Reminc. (App. 52a). This unsecured claim and Reminc's counterclaim were the subject of a two-day trial held before the United States Bankruptcy Court on January 29 and 30, 1980.

Central to both the USE claim and the Reminc counterclaim was a single issue: whether USE installed the elevator system in accordance with contract specifications. The parties introduced severely conflicting testimony on this point. USE witnesses testified that the elevators operated within industry

standards. None of these witnesses admitted to observing any serious performance problems. Reminc, for its part, presented the testimony of a Xerox Corporation employee who, as facility manager for the prime tenant, monitored complaints about the elevators on a daily basis. Included among the numerous complaints he had logged were a constant bouncing motion of the elevators at landings, stops above or below floor level, failures to stop at floors selected by passengers, large passenger lines in the lobby, and occasional free falls of one or two floors. The same or similar phenomena were observed by the elevator adjusters who ultimately replaced USE personnel and by two experts hired by Reminc to devise a plan for correcting the system's deficiencies. Anchoring Reminc's case was a memorandum prepared by L. William ("Bill") Cork, the first elevator adjustor USE assigned to correct problems at the Xerox Building. DX NN (App. 56a). The Cork memorandum, dated October 13, 1975, not only confirmed, from the mouth of a USE employee, the same performance problems observed by Reminc's live witnesses, but it made clear precisely why these problems existed.

Cork's own words elegantly framed the stark reality of USE's failure:

> In conclusion, our most serious problem is still present. The loading car releveling makes the people afraid of the elevator. The car bouncing keeps this fear alive. The multiplex controller still has many problems. We have added many aspirins to relieve the pain, but we have not fixed the broken leg.

DX NN, 6 (App. 63a).

The Bankruptcy Court determined that USE substantially performed its contract obligations. In evaluating the parties' conflicting contentions about the elevators' performance, the Bankruptcy Court ruled that Cork's memorandum was inadmissible hearsay. It then found the USE evidence to be the more credible. The Bankruptcy Court ruled also that the assignment to Reminc of Citcon's choses in action against subcontractors rendered Reminc affirmatively liable to USE for the contract price. Finally, it ruled that USE could assert a

contract claim against Reminc even though the assignment on which the claim was predicated did not occur until after the filing of the bankruptcy petition. (App. 7a-38a).

The District Court affirmed in a brief oral opinion. Judge Bryan considered the Bankruptcy Court's ultimate findings of fact to be supported by "sufficient evidence" (App. 5a). The District Court held that the Cork memorandum was improperly excluded, but that the error was harmless. (App. 5a).

Reminc appealed to the United States Court of Appeals for the Fourth Circuit. The Court of Appeals also ruled that any error in excluding from evidence the Cork memorandum was harmless. This ruling was grounded on the fact that "[d]uring [Cork's] deposition counsel for Reminc was free to question Cork about the memorandum and did so in some detail."[1] (App. 2a-3a). With respect to the other issues briefed by Reminc, the Court of Appeals stated,

> Reminc also raises with us issues concerning (1) the assignment of liabilities by Citcon, (2) USE's status as a general creditor, (3) the sufficiency of the evidence to support a finding that USE performed its contract in a workmanlike manner and (4) the constitutionality of Bankruptcy Rule 810. A review of the record, the bankruptcy court's opinion and the district court's affirmance discloses that these issues are without merit. (App. 3a)

REASONS FOR ALLOWING THE WRIT

1. IN HOLDING THAT BANKRUPTCY RULE 810, PRECLUDING DE NOVO REVIEW BY AN ARTICLE III JUDGE, IS CONSTITUTIONAL WHEN APPLIED TO A COMMON LAW CONTRACT CLAIM AGAINST A DEBTOR IN A PROCEEDING UNDER THE BANKRUPTCY ACT OF 1898, THE COURT OF APPEALS

[1] At the time of trial, Cork was not employed by USE and lived in California. Reminc deposed Cork in California and offered the deposition in lieu of live testimony.

DECIDED AN IMPORTANT QUESTION OF LAW, NOT YET DECIDED BY THIS COURT, IN A WAY THAT CONFLICTS WITH THE COURT'S DECISION IN *NORTHERN PIPELINE CONSTRUCTION CO. V. MARATHON PIPE LINE CO.*

In *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, __U.S.__, 50 U.S.L.W. 4892 (U.S. June 28, 1982), which addressed the Bankruptcy Reform Act of 1978, the Court expressly left undecided the constitutional propriety of adjudications by Article I officers under the Bankruptcy Act of 1898. 50 U.S.L.W. at 4900 n.31. This question remains crucial to bankruptcy proceedings initiated prior to the effective date of the 1978 Act.[2] The importance of the question as a matter of constitutional law is manifest, and its prompt resolution by this Court would greatly enhance the orderly resolution of those proceedings which it affects. As of March 31, 1982, some 65,000 cases filed under the 1898 Act were still pending.[3]

The Court's opinions in *Northern Pipeline* lead inescapably to the conclusion that the "clearly erroneous" deference which Bankruptcy Rule 810 accords to findings by the Bankruptcy Court cannot pass constitutional muster where a common law contract claim within the exclusive federal jurisdiction established by the 1898 Act is at stake.[4] The fatal defects in this

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[2] The Bankruptcy Reform Act of 1978 became effective on October 1, 1979. P.L. 95-598 § 402, 11 U.S.C. prec. § 101 note (Supp. III 1979). All cases commenced before that date are governed by the provisions of the old act for their duration. *Id.* § 403(a).

[3] Administrative Office of the United States Courts, *Federal Judicial Workload Statistics for the Twelve Month Period Ended March 31, 1982*, Table F-1 (1982).

[4] Under the Bankruptcy Act of 1898, all claims against a bankruptcy debtor's estate are within the jurisdiction of the Bankruptcy Court. § 2, 11 U.S.C. §§ 11(a)(2), (7), (12), (15) (1976) (repealed). Because bankruptcy proceedings stay all actions, including those in state courts, against the debtor and ultimately discharge all preexisting obligations of the debtor, the federal jurisdiction over claims against the debtor is exclusive. §§ 11, 14, 11 U.S.C. §§ 29, 32 (1976) (repealed). Claims by the debtor against third parties, other than counterclaims, come within the Bankruptcy Court's jurisdiction only if the third party consents. § 2, 11 U.S.C. § 11(a) (7) (1976) (repealed). Whether such claims may be adjudicated by a legislative court is not at issue here.

scheme are precisely identical to those inherent in the Bankruptcy Reform Act of 1978: the adjudication does not come within one of the three narrow situations in which Congress may create a legislative court, and the Bankruptcy Court does not function as a mere adjunct of the District Court.

Whatever the authority of Congress to create legislative courts, it plainly does not extend to the common law contract claim adjudicated in this case. The breach of contract claim USE asserted against Reminc arises wholly under state law, is subject to no federal rule of decision, is subject to the traditional common law mode of adjudication, and is before a federal court only because Reminc filed a bankruptcy petition. The claim, in short, is of the same type as that which the Court in *Northern Pipeline* found to be unsuitable for determination by an Article I tribunal. 50 U.S.L.W. at 4894, 4898 (Brennan, J); *id.* at 4903 (Rhenquist, J., concurring).

The Bankruptcy Court under the 1898 Act similarly is not an adjunct of the District Court, as long as Rule 810 precludes de novo review of its findings.[5] Rule 810, both by effect and by design, places the power of decision in the Bankruptcy Court. It limits Article III Courts to a strictly appellate role. This appellate supervision is inadequate to preserve the separation of legislative and judicial powers which the framers sought to accomplish through Article III. *Northern Pipeline Construction Co. v. Marathon Pipe Line Co.*, 50 U.S.L.W. at 4901-02 & n.39 (Brennan, J.); *id.* at 4903 (Rhenquist, J., concurring); *See United States v. Raddatz*, 447 U.S. 667, 682-84 (1980); *id.* at 707-12 (Marshall, J., dissenting). As stated by Mr. Justice Rhenquist in *Northern Pipeline*,

> I am likewise of the opinion that the extent of review by Art. III courts provided on appeal from a decision of the Bankruptcy Court in a case such as Northern's does not save the grant of authority to the latter under the rule espoused in *Crowell v. Benson*, 285

[5] The Bankruptcy Act of 1898 does not itself require that any deference be given to Bankruptcy Court findings. § 2(a), 11 U.S.C. § 11(a)(10) (1976) (repealed). Only Rule 810 precludes de novo review by the District Court.

> U.S. 22 (1932). All matters of fact and law in whatever domains of the law to which the parties' dispute may lead are to be resolved by the Bankruptcy Court in the first instance, with only traditional appellate review apparently contemplated by Art. III courts. Acting in this manner the Bankruptcy Court is not an "adjunct" of either the District Court or the Court of Appeals.

50 U.S.L.W. at 4903.

In light of the pronounced incompatibility of Rule 810 with the views expressed by the Court in *Northern Pipeline*, Reminc respectfully suggests that the Court not only grant the petition, but summarily vacate the judgment below and remand the case with directions for de novo proceedings in the District Court. If such action were taken, the additional questions raised in the petition would become moot.

2. THE COURT OF APPEALS' HOLDING THAT ORAL TESTIMONY RENDERS HARMLESS THE ERRONEOUS EXCLUSION OF A DOCUMENT IS IN CONFLICT WITH THIS COURT'S DECISION IN *GORDON V. UNITED STATES* AND CALLS FOR AN EXERCISE OF THIS COURT'S POWER OF SUPERVISION

There can be no serious doubt that the Bankruptcy Court erroneously excluded the Cork memorandum from evidence. Indeed, the memorandum was admissible on at least three grounds. First, and foremost, it was an admission of a party opponent. Fed. R. Evid. 801(d)(2)(D).[6] In addition, it was both a business record and past recollection recorded. Fed. R. Evid. 803(5), (6).

The Court of Appeals' conclusion that the opportunity to examine Cork about the contents of his memorandum rendered its exclusion harmless is in conflict with this Court's decision in *Gordon v. United States*, 344 U.S. 414 (1953). Ruling that the

[6] The Federal Rules of Evidence are applicable to bankruptcy proceedings. Bankruptcy Rule 917.

judgment below had to be reversed due to the exclusion of documentary evidence, Justice Jackson stated for a unanimous Court:

> The Court of Appeals affirmed on the ground that Marshall's admission, on cross-examination, of the implicit contradiction between the documents and his testimony removed the need for resort to the statements and the admission was all the accused were entitled to demand. We cannot agree. We think that an admission that a contradiction is contained in a writing should not bar admission of the document itself in evidence, providing it meets all other requirements of admissibility and no valid claim of privilege is raised against it. The elementary wisdom of the best evidence rule rests on the fact that the doument is a more reliable, complete and accurate source of information as to its contents and meaning than anyone's description and this is no less true as to the extent and circumstances of a contradiction. We hold that the accused is entitled to the application of that rule, not merely because it will emphasize the contradiction to the jury, but because it will best inform them as to the document's impeaching weight and significance.

344 U.S. 414, 420-21 (1953) (footnotes omitted); *cf.* Fed. R. Evid. 1002, 1004 (best evidence rule).

Where, as here, the excluded document was not merely intended for impeachment, but constituted part of Reminc's affirmative proof, an even stronger case for reversal exists.

What is more, the holding that the mere opportunity to elicit oral testimony concerning a writing remedies the writing's exclusion will have serious detrimental consequences on the conduct of litigation in the federal courts. The holding allows a trial judge, without reversal, to exclude a document which would be recognized as patently admissible by any second-year law student merely because the document's author was deposed. Under such a rule, responsible counsel expecting to use a deposition at trial would have no choice but painstakingly to

review each and every line of each and every document the deponent is shown. Not only would the unnecessary expense and burden associated with such a practice be immense, but it would mark such a substantial departure from the accepted and usual course of judicial proceedings as to call for an exercise of this Court's power of supervision.[7]

3. THE COURT OF APPEALS' HOLDING THAT AN ASSIGNEE OF A CONTRACT RIGHT BECOMES AFFIRMATIVELY LIABLE FOR CONTRACT OBLIGATIONS IS SO CLEARLY WRONG AS TO CALL FOR AN EXERCISE OF THIS COURT'S POWER OF SUPERVISION

Few principles of American jurisprudence are more firmly established than that a contract right may be assigned and that the assignee of a right does not become liable for any contract obligation of the assignor. As stated by the United States Court of Appeals for the Ninth Circuit,

> Merely as assignee one does not become affirmatively liable for a deficit in the accounts between his assignor and the other party to the assigned contract. Any such liability would have to be based upon an affirmative assumption, by the assignee, of the obligations of his assignor on the contract, or upon some independent contractual agreement.

United States ex rel. White v. Thompson & Georgeson, Inc., 346 F.2d 865, 869 (9th Cir. 1965); *see, e.g., Urban v. Phy*, 24 F.2d 494, 495 (9th Cir. 1928); *Ebling Brewing Co. v. Cereal Products Co.*, 6 F.2d 984, 985 (2d Cir. 1925); *Chatham Pharmaceuticals Inc. v. Angier Chemical Co.*, 347 Mass. 208, 209, 196 N.E.2d 852, 853 (1964); *Keyes v. Scharer*, 14 Mich. App. 68, 72, 165 N.W.2d 498, 501 (Ct. App. 1968); *Falkenstern v. Herman Kussy Co.*, 137 N.J.L. 200, 202, 59 A.2d 372, 374 (Ct. of Errors

[7] The record is clear that the complete contents of the memorandum were not actually in the deposition transcript. Many of Cork's answers merely incorporated portions of the document by reference. These portions of the transcript are wholly uninformative in the absence of the document.

& Appeals 1948); *Daniels v. Parker*, 209 Or. 419, 422-23, 306 P.2d 735, 736 (1957); *Shepard v. Commercial Credit Corp.*, 123 Vt. 106, 108, 183 A.2d 525, 528 (1962); 4 A. Corbin, *Contracts* § 906, p. 627 (1951) ("If the assignee has not contracted to perform the duties of the assignor, no action can be maintained against him, either by the assignor, or by the third party as a beneficiary."); 3 S. Williston, *A Treatise on the Law of Contracts* § 418A, p. 105 (3d ed. 1960) ("It is doubtless possible for a party to a bilateral contract to assign only the rights that will accrue to him under the contract without delegating performance of the duties."); *cf.* Williston, *supra* § 407, at 13 ("A clear conception of the law governing assignment of contracts can be obtained only by sharply distinguishing between attempted assignments of rights and of duties.").

The ability of an assignee to recover on a right, of course, is diminished by such defenses or claims as the obligor may have against the assignor. *Restatement (Second) of Contracts* § 336 (1981). These defenses and claims inherently limit the assignor's right to receive payment from the obligor. The assignor can convey to the assignee no more than he himself has. *Id.* Comment b.

A mere limitation on a right, however, does not afford an affirmative basis for recovery against the holder of the right. According to the drafters of the *Restatement (Second) of Contracts,*

> In appropriate circumstances the obligor may use defensively against an assignee an offsetting claim against the assignor, *although the assignee is not subject to affirmative liability on such a claim unless he contracts to assume such liability.*

Id. Comment c (emphasis added); *see* G. Grismore, *Principles of the Law of Contracts* § 259, p. 424 n.99 (rev. ed. 1965).

The Bankruptcy Court ruled that Reminc, which had use of the elevators, had an equitable obligation to pay for them. Memorandum Opinion, 11-12 (App. 18a-19a). Apart from the obvious inconsistency of this ruling with the applicable legal principles, there was clearly no windfall to Reminc here.

Reminc's entitlement to the elevators, and its obligation to pay for them, derive from the general contract with Citcon. Reminc made all required payments under the general contract and finally settled all accounts with Citcon. There was no evidence whatsoever that Reminc had any interest in or control over Citcon or that the general contractor's accounts were not settled on an arm's length basis. Citcon's ultimate failure or inability to pay is nothing more or less than the business and credit risk USE accepted when it signed the subcontract. In the final analysis, the Bankruptcy Court did not prevent a windfall, but awarded one to USE.[8]

4. THE COURT OF APPEALS' HOLDING THAT USE COULD BECOME A GENERAL CREDITOR OF REMINC AFTER REMINC PETITIONED FOR BANKRUPTCY IS IN CONFLICT WITH THIS COURT'S DECISION IN *UNITED STATES v. MARXEN.*

The Bankruptcy Act of 1898 fixes creditors' rights at the time the petition commencing bankruptcy proceedings is filed. *See, e.g., United States v. Marxen,* 307 U.S. 200, 207 (1939); *White v. Stump,* 266 U.S. 310, 313 (1924); *Everett v. Judson,* 228 U.S. 474, 478, 479 (1913); *Acme Harvester Co. v. Beekman Lumber Co.,* 222 U.S. 300, 307, 308 (1911); *In re C.H. Earle, Inc.,* 2 F. Supp. 15, 16 (E.D.N.Y. 1932), *aff'd,* 65 F.2d 1013 (2d Cir.), *cert. denied sub nom. Globe Indemnity Co. v. C.H. Earle, Inc.,* 290 U.S. 674 (1933). Consequently, a party cannot be recognized as a general creditor in a bankruptcy proceeding unless he extended credit to and thereby had a claim against the bankrupt prior to the bankruptcy petition. For bankruptcy purposes, a claim is defined as "a cause of action or ground for liability. . . ." *Continental Motors Corp. v. Morris,* 169 F.2d 315,

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[8] *Fiberchem, Inc. v. General Plastics Corp.*, 495 F.2d 737 (9th Cir. 1974), relied on by the Bankruptcy Court, is inapposite. The *Fiberchem* court held that an assignee of a contract right to make a sale cannot collect the proceeds of the sale without paying a commission to the third party sales agent. The court merely protected the latent equities of the third party, who was not a signatory to either the original contract or the assignment. Such protection is routine. *See* Williston, *supra,* § 438; *Restatement, supra,* § 343. There is no comparable third party, and no comparable latent equity, here.

316, (10th Cir. 1948); *see In re Hayes,* 127 F. Supp. 514, 516 (D. Alaska 1955).

USE's original claim was based on the Virginia mechanic's lein statute. Va. Code § 43-7 (1981). This was a purely statutory right of action, wholly separate from USE's contract rights against Citcon. *See Coleman v. Pearman,* 159 Va. 72, 165 S.E. 371 (1932). The unsecured claim which was ultimately allowed by the Bankruptcy Court was based solely on the contract obligations purportedly assigned to Reminc by Citcon. The assignment did not occur, and the claim was not asserted, until well after the bankruptcy petition was filed.

The Bankruptcy Court permitted the claim by completely misreading this Court's decision in *United States v. Marxen.* In *Marxen,* the United States was assigned a right against a debtor after the debtor had petitioned for bankruptcy. The Court denied the United States the preference normally accorded its claims because the assignor—who held the debt when the petition was filed—would have had no such preference. The Bankruptcy Court here reasoned that since the United States' claim in *Marxen* was not extinguished, but treated as a general unsecured claim, USE's claim should also be treated as a general unsecured claim. (App. 12a-13a). This overlooks the very essence of the *Marxen* holding: the only claim that could be pressed was the one which existed when the petition was filed. USE's unsecured claim did not arise, if at all, until after the petition. *Marxen* requires not an affirmance, but a reversal.

CONCLUSION

In light of *Northern Pipeline*, the petition for a writ of certiorari should be granted and the judgment below summarily vacated. Should the Court regard summary action as inappropriate, the writ should be granted for all of the reasons set forth above.

Respectfully submitted,

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